

Office of Chief Counsel
Internal Revenue Service
Memorandum

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to: Rick Ward
Small Business/Self-Employed
Program Manager
(SBSE:PSP:INTL)

from: M. Grace Fleeman, Senior Technical Reviewer, CC:INTL:1
Edward R. Barret, Assistant to the Branch Chief, CC:INTL:1

subject: Notice of Withdrawal of Ruling Request PLR-101761-06

In accordance with section 7.07(2) of Rev. Proc. 2006-1, 2006-1 I.R.B. 1, we are providing you with notification of a taxpayer withdrawal of a private letter ruling request. On July 26, 2006, Taxpayer's representative withdrew the above-referenced request for a private letter ruling after this office advised Taxpayer and Taxpayer's representative of its tentative adverse position. Following is a brief discussion of the issue, facts, applicable law, and the reason for this office's tentative adverse position. A copy of Taxpayer's request is attached. This memorandum is not binding on Examination or Appeals and is not a final case determination. This document is not to be used or cited as precedent.

LEGEND

Taxpayer =

Country X =

ISSUE

Taxpayer requested a ruling that income received by residents of Country X under life insurance and annuity contracts issued by Taxpayer does not constitute U.S. source income that is subject to 30-percent tax and withholding under sections 871(a) and 1441 or 15-percent withholding under the United States-Country X income tax treaty¹ (the “Treaty”).

CONCLUSION

This office’s adverse position was based on the following. Under Rev. Rul. 2004-75, distributions received by residents of Country X under life insurance and annuity contracts issued by Taxpayer are U.S. source income. Under Article _____ of the Treaty, periodic distributions under the annuity contracts issued by Taxpayer to Country X residents are generally subject to 15-percent U.S. withholding tax. Amounts withdrawn from the accumulation value of the annuity contracts and distributions to Country X residents under Taxpayer-issued life insurance contracts (including withdrawals from the cash value of the life insurance contracts) are covered by Article _____ of the Treaty and are generally subject to 30-percent U.S. withholding tax.²

FACTS

Taxpayer is a State A corporation that conducts business in the United States and Country X. Taxpayer sells a number of different types of insurance products to individuals living in the United States and Country X. Taxpayer represents that these insurance products are life insurance and annuity contracts under the Internal Revenue Code.

Residents of Country X pay premiums to Taxpayer in exchange for the benefits set forth in the relevant life insurance and annuity contracts. Under a life insurance contract, Taxpayer generally agrees, in exchange for premiums, to pay the face amount of a certificate (less any outstanding loan balance) to a beneficiary upon the death of the insured. Under an annuity contract, Taxpayer generally agrees, in exchange for premiums, to pay a certain amount each year to the owner of the contract based on the selection of a payment option by the contract owner.

Taxpayer represents that premiums from sales to residents of Country X of Taxpayer insurance products are deposited in a Country X account and are invested in Country X income-producing assets, such as stocks and bonds.

1

² If the Country X resident who receives a distribution under a Taxpayer-issued annuity or life insurance contract is a U.S. citizen or, in certain cases, a former U.S. citizen, such distribution would not be subject to U.S. withholding tax, but the individual would be subject to net-basis U.S. tax on the portion of the distribution that constitutes gross income for purposes of U.S. tax law.

The annuity contracts issued by Taxpayer to Country X residents have accumulation values. The life insurance contracts issued by Taxpayer to Country X residents may have cash values depending on the type of contract. Individuals resident in Country X may withdraw the accumulation values of their annuity contracts or the cash values of their life insurance contracts.

LAW AND ANALYSIS

Rev. Rul. 2004-75, 2004-2 C.B. 109,³ held in relevant part that income received by nonresident alien individuals under life insurance and annuity contracts issued by a foreign branch of a U.S. life insurance company is U.S. source fixed or determinable annual or periodical income (“FDAP income”) that is subject to 30-percent tax and withholding under sections 871(a) and 1441.

Under the facts of the present case, the same legal analysis set forth in Rev. Rul. 2004-75 applies. Thus, for purposes of U.S. domestic law, distributions received by residents of Country X under the life insurance and annuity contracts issued by Taxpayer are U.S. source income. In contrast to the factual scenario in Rev. Rul. 2004-75, there is an income tax treaty in force between the United States and Country X. Accordingly, the terms of the Treaty govern the U.S. taxation of distributions under Taxpayer-issued life insurance and annuity contracts in the hands of residents of Country X.

As explained in the Technical Explanation (TE) to Article (Pensions and Annuities), Article does not provide rules to determine where annuities and similar amounts arise.⁴ The Treaty similarly does not provide source rules for distributions under life insurance contracts. For purposes of the Treaty, the source of distributions under the annuity and life insurance contracts issued by Taxpayer is thus determined under U.S. law (*i.e.*, under Rev. Rul. 2004-75). See Article .

Paragraph of Article of the Treaty applies to determine how periodic distributions under the annuity contracts issued by Taxpayer to Country X residents are taxed in the United States. Under sub-paragraph of Article , the periodic annuity distributions are subject to 15-percent U.S. withholding tax on the portion of the distribution that would not be excluded from U.S. taxable income if the beneficial owner were a resident of the United States.

Article (Other Income) of the Treaty applies to determine how amounts withdrawn from the accumulation value of the annuity contracts⁵ and distributions under the life

³ Rev. Rul. 2004-75 was amplified by Rev. Rul. 2004-97, 2004-2 C.B. 516.

⁴ The TE to Article notes that the provisions of paragraph of Article (General Definitions) are used for this purpose.

⁵ Paragraph of Article provides that, for purposes of the Treaty, the term “annuities” means a stated sum paid periodically at stated times during life or during a specified number of years, under an obligation to make the payments in return for adequate and full consideration (other than services

insurance contracts (including withdrawals from the cash value of the life insurance contracts) are taxed in the United States. Because Article does not contain a limit on the source state rate of tax, the (U.S. source) amounts withdrawn from the accumulation value of the annuity contracts and the (U.S. source) distributions under the life insurance contracts would be subject to 30-percent U.S. withholding tax, to the extent that such amounts constitute gross income for purposes of U.S. tax law.

The Treaty's saving clause (paragraph of Article) permits the United States to tax its citizens and certain former citizens as if there were no Treaty between the United States and Country X. Accordingly, residents of Country X who are U.S. citizens or, in certain cases, former U.S. citizens would not be subject to U.S. withholding tax with respect to distributions under Taxpayer-issued life insurance and annuity contracts, but would be subject to net-basis U.S. tax on such distributions to the extent that the distributions constitute gross income for purposes of U.S. tax law.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call [01203 646000](tel:01203 646000) if you have any further questions.

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Branch 1
Office of Associate Chief Counsel (International)

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rendered), but does not include a payment that is not a periodic payment. Amounts withdrawn from the accumulation value of the annuity contracts are not periodic payments and are thus not covered by Article